

BEFORE THE  
STATE OF NEW JERSEY  
BOARD OF PUBLIC UTILITIES

IN THE MATTER OF THE PETITION OF  
NEW JERSEY-AMERICAN WATER COMPANY, INC.  
FOR APPROVAL OF INCREASED TARIFF RATES  
AND CHARGES FOR WATER AND WASTEWATER SERVICE,  
CHANGE IN DEPRECIATION RATES AND  
OTHER TARIFF MODIFICATIONS

BPU Docket No. WR1709\_\_\_\_\_

**DIRECT TESTIMONY OF**

**ROBERT V. MUSTICH**

**PUBLIC VERSION**

**Exhibit PT-19**



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NEW JERSEY-AMERICAN WATER COMPANY, INC.1    **I.     INTRODUCTION**2    **1. Q. Please provide your name, position and business address.**

3        A. My name is Robert V. Mustich. I am Managing Director and the U.S. East Region  
4        Line of Business Leader, Rewards for Willis Towers Watson. Willis Towers Watson  
5        is a leading global professional services company which has 40,000 associates  
6        throughout the world, and offers solutions in the areas of corporate risk and broking;  
7        human capital and benefits; health care exchange solutions; and investment, risk, and  
8        reinsurance. My business address is 800 North Glebe Road, Arlington, VA 22203.

9    **2. Q. Please state your educational and professional background and experience.**

10       A. I graduated from American University with a BS/BA in Human Resources  
11       Management. I have over 25 years of industry and compensation consulting services  
12       experience, have been with Willis Towers Watson for over 20 years, and have  
13       assisted management and Boards of Directors at many companies in designing and  
14       assessing total compensation programs. Since joining the firm in 1997, I have  
15       consulted with numerous utilities and currently serve as U.S. East Region Line of  
16       Business Leader, Rewards in addition to being a senior member of our utilities  
17       industry practice. I have conducted competitive assessments of total compensation  
18       for numerous public utilities throughout the U.S. Prior to joining Willis Towers  
19       Watson, I was a senior compensation consultant for PricewaterhouseCoopers  
20       (formally Coopers and Lybrand, LLP) performing similar compensation consulting  
21       services for clients. Prior to that, I held corporate senior staff compensation and  
22       benefits positions.

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1    **3. Q. Have Willis Towers Watson and you performed similar analyses in the past?**

2        A. Yes. Willis Towers Watson and I have conducted similar competitive compensation  
3        studies for other utility clients.

4    **4. Q. Please explain Willis Towers Watson's experience in providing compensation**  
5        **and benefits consulting services to organizations like New Jersey-American**  
6        **Water Company ("NJAWC").**

7        A. Willis Towers Watson has extensive experience serving clients in the utility industry,  
8        having served over 100 utilities in the U.S. within the last year. Because we invest so  
9        heavily in our utility industry capabilities, we have rich competitive industry  
10       compensation and benefits information that enables us to benchmark NJAWC against  
11       similar companies in the U.S. Given Willis Towers Watson's breadth and depth of  
12       resources, we are frequently engaged by companies to evaluate the competitiveness of  
13       their compensation philosophy, compensation and benefit levels, at-risk  
14       compensation design and pay structures, and other consulting services.

15    **II.    DEFINITIONS**

16    **5. Q. Can you please identify some of the key definitions that you will need to**  
17        **reference as part of your testimony?**

18        A. Yes.

19    **6. Q. More specifically, please define Target Total Cash Compensation.**

20        A. Target Total Cash Compensation represents the sum of base salary plus target short-  
21       term at-risk compensation.

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1    **7. Q. Please define Target Total Direct Compensation.**

2        A. Target Total Direct Compensation represents the sum of base salary, plus target short-  
3        term at-risk compensation, plus long-term at-risk compensation.

4    **III.    PURPOSE OF TESTIMONY**

5    **8. Q. What is the purpose of your testimony?**

6        A. The purpose of my testimony is to demonstrate that the target total direct  
7        compensation provided to NJAWC's at-risk compensation eligible employees, when  
8        viewed against the markets for talent for employees in similar positions, is within the  
9        competitive range of the market based on the company's stated compensation  
10       philosophy. Willis Towers Watson specifically focused on the following aspects of  
11       NJAWC's program:

- 12       • Total compensation philosophy;
- 13       • Competitive market positioning of target total direct compensation (base salary  
14       plus short-term at-risk compensation plus long-term at-risk compensation)
- 15       • Design of short-term at-risk compensation program; and
- 16       • Design of long-term at-risk compensation program.

17    **IV.    OVERVIEW OF TOTAL COMPENSATION PHILOSOPHY**

18    **9. Q. Does NJAWC have a defined compensation philosophy?**

19       A. Yes, American Water Works Company, Inc. ("American Water") has a defined  
20       compensation philosophy which is applicable to NJAWC.

NEW JERSEY-AMERICAN WATER COMPANY, INC.**10. Q. How would you define the parent company's compensation philosophy?**

A. American Water's compensation philosophy is to generally pay salaries that are competitive with those of comparable organizations for jobs of similar responsibility. To carry out this philosophy, American Water's objective is to target total direct compensation (base, short-term at-risk compensation, and long-term at-risk compensation) at the median (50th percentile) of the market with greater earning opportunity for exceptional performance for fully qualified individuals.

**11. Q. How does this compensation philosophy compare with other utilities?**

A. Willis Towers Watson examined the proxy statements for two peer groups: (1) Large Utility Peer Group, 15 publicly-traded utilities comparable in size to American Water (revenues range from ½ to 2.5 times American Water's 2016 revenues of \$3.3 billion), as disclosed in the company's March 27, 2017 proxy statement, and (2) Small Utility Peer Group, 12 publicly-traded utilities comparable in size to NJAWC (revenues range from \$348-\$1,461M, compared to NJAWC's 2016 revenue of \$730M). Based on our review, we believe American Water's compensation philosophy is well-aligned with utility peers, as a majority of both Large Utility Peer Group companies (14 of 15, 93%) and Small Utility Peer Group companies (10 of 12, 83%) target the market median (50th percentile) for some or all pay elements. Our consulting experience also suggests that American Water's median (50th percentile) pay philosophy is comparable to typical market practice found in general industry.



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1 **V. SUMMARY OF WILLIS TOWERS WATSON’S TOTAL COMPENSATION**  
 2 **STUDY**

3 **12. Q. Did you conduct a compensation study of NJAWC’s compensation program?**

4 A. Yes, and a copy of the Study is included as Schedule RVM-1 to my testimony.

5 **13. Q. Please describe how the study was conducted.**

6 A. Willis Towers Watson utilized three data sources to assess NJAWC’s compensation  
 7 program: (1) As we did in assessing American Water’s total compensation  
 8 philosophy, we assessed the design of its short-term at-risk and long-term at-risk  
 9 compensation programs using proxy disclosures of groups of public utilities referred  
 10 to as the (1) Large Utility Peer Group and (2) Small Utility Peer Group, and (3)  
 11 competitive market positioning of NJAWC’s target total direct compensation levels  
 12 was compared to Willis Towers Watson published compensation surveys.

13 **14. Q. How did you define “competitive” for the purposes of your compensation study?**

14 A. Willis Towers Watson and typical market practice define an element of total  
 15 compensation as being competitive if it falls in a range that extends between 10%  
 16 below to 10% above the market median level of total compensation.

17 **15. Q. Please describe how you assessed the competitiveness of NJAWC’s target total**  
 18 **direct compensation levels.**

19 A. Willis Towers Watson assessed the competitiveness of target total direct  
 20 compensation provided by NJAWC to its short-term at-risk eligible population based  
 21 on a selection of NJAWC jobs (“benchmark jobs”). Benchmark jobs are those

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1 positions that are common across comparable organizations and for which  
2 compensation data are available from published surveys.

3 To conduct this analysis we reviewed compensation data provided to us by NJAWC  
4 and examined Willis Towers Watson's compensation surveys in our Compensation  
5 Databank (CDB). These surveys are comprised of compensation data from over 1,000  
6 U.S. based companies, and Willis Towers Watson has been conducting these surveys  
7 for over 20 years.

8 NJAWC's current compensation levels were compared to the market 50th percentile  
9 (market median) for two different market perspectives to determine the  
10 competitiveness of pay and to validate the alignment with American Water's current  
11 compensation philosophy (targeting compensation at the 50th percentile of market).

12 Willis Towers Watson's assessment of benchmark jobs represents approximately  
13 70% of the population of NJAWC employees as of April 7, 2017, who are eligible for  
14 at-risk compensation. Specific details regarding our study, which includes a detailed  
15 description of the study methodology, are included in Schedule RVM-1.

16 **16. Q. How did you derive 50th percentile (median) market values?**

17 A. To derive 50th percentile (median) market values, Willis Towers Watson weighted  
18 energy services (primarily utilities) and general industry survey data 60% and 40%  
19 respectively to place a greater weight on the energy services market data since this  
20 includes regulated entities most similar to NJAWC for positions that are not industry  
21 specific. Given that these positions can be recruited or lost to companies in any

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1 industry, the use of general industry survey data ensures that non-industry specific  
2 positions are being compensated competitively. Industry specific positions were  
3 compared only to energy services industry data.

4 **17. Q. Please describe how you determined the competitiveness of NJAWC's target**  
5 **total direct compensation?**

6 A. Two different market perspectives were examined to validate the competitiveness of  
7 NJAWC's target total direct compensation.

8 A national market perspective was examined which consisted of the entire population  
9 of survey participants in Willis Towers Watson's Energy Services and General  
10 Industry databases. This perspective represents a U.S. national compensation  
11 perspective and is aligned with American Water's compensation philosophy.

12 A Mid-Atlantic regional perspective including Delaware, New Jersey, New York, and  
13 Pennsylvania labor markets was also examined, which consisted of the same entire  
14 survey participant population from Willis Towers Watson's Energy Services Industry  
15 and General Industry databases but was customized to identify a Mid-Atlantic-  
16 specific geographic dataset. This dataset identified employees that work in the four  
17 states listed above for companies headquartered anywhere in the United States.

18 **18. Q. What were the compensation study results from the national perspective?**

19 A. Using a weighted average of all positions reviewed, NJAWC's target total direct  
20 compensation, as reported in Exhibit 1 (below), is at the low end of the range of  
21 competitive market median by being [BEGIN CONFIDENTIAL] [REDACTED] [END  
22 CONFIDENTIAL] market median. Again, Willis Towers Watson and typical market

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practice considers market competitiveness to be a result that falls within plus or minus 10% of median range.

**Exhibit 1**

Summary of New Jersey American Water's Target Total Direct Compensation vs. Market Median (National Market Perspective)		
Base Pay	Target Total Cash Compensation	Target Total Direct Compensation
[BEGIN CONFIDENTIAL] [REDACTED]	[REDACTED]	[REDACTED] [END CONFIDENTIAL]

**19. Q. What were the compensation study results from the Mid-Atlantic Regional perspective?**

A. NJAWC's target total direct compensation is within the market median range, as reported in Exhibit 2, because it is [BEGIN CONFIDENTIAL] [REDACTED] [END CONFIDENTIAL] (represents a weighted average of all positions reviewed) below the market median.

**Exhibit 2**

Summary of New Jersey American Water's Target Total Direct Compensation vs. Market Median (Mid-Atlantic Regional Market Perspective)		
Base Pay	Target Total Cash Compensation	Target Total Direct Compensation
[BEGIN CONFIDENTIAL] [REDACTED]	[REDACTED]	[REDACTED] [END CONFIDENTIAL]

**20. Q. What would be the impact on the competitiveness of NJAWC's target total direct compensation if short-term and long-term at risk compensation were not part of its compensation program?**

A. If we compare NJAWC's total compensation program excluding at-risk compensation (that is, base salary alone) to market pay levels that include at-risk compensation, as reported in Exhibits 3 and 4, NJAWC's target total direct compensation would not be competitive because it would [BEGIN CONFIDENTIAL] [REDACTED] [END CONFIDENTIAL] median from a national perspective and [BEGIN CONFIDENTIAL] [REDACTED] [END CONFIDENTIAL] median from a Mid-Atlantic Regional perspective.

Summary of New Jersey American Water's NJAW Base Salary Only vs. Market Median (National Market Perspective)		
Base Pay	Target Total Cash Compensation	Target Total Direct Compensation
[BEGIN CONFIDENTIAL] [REDACTED]	[REDACTED]	[REDACTED] [END CONFIDENTIAL]

Summary of New Jersey American Water's NJAW Base Salary Only vs. Market Median (Mid-Atlantic Regional Market Perspective)		
Base Pay	Target Total Cash Compensation	Target Total Direct Compensation
[BEGIN CONFIDENTIAL] [REDACTED]	[REDACTED]	[REDACTED] [END CONFIDENTIAL]

A. No. NJAWC employees are generally within the range of market median when at risk compensation is included in the compensation program.

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**VI. SUMMARY OF WILLIS TOWERS WATSON'S SHORT-TERM AT-RISK  
PROGRAM ASSESSMENT**

**22. Q. Did you conduct an assessment of American Water's short-term at-risk program?**

A. Yes.

**23. Q. What was the purpose of your assessment?**

A. This assessment was completed to compare the design of American Water's short-term at risk program (that is applicable to NJAWC) and its various elements to market practice.

**24. Q. What were the findings of the assessment?**

A. Overall our review indicates that American Water's short-term incentive program is comparable to and competitive with designs of utility peers, based on a review of the Large Utility Peer Group and the Small Utility Peer Group that I referenced earlier. Like American Water, every company reviewed has a short-term at-risk compensation program that it uses to help attract, motivate and retain critically skilled employees needed to successfully run the business. Companies design their short-term at-risk compensation programs to align with their business strategies and circumstances, so there tends to be a range of practices regarding how the programs are designed.

American Water's short-term at-risk compensation program assesses performance using a balanced scorecard approach, incorporating financial, safety, customer satisfaction, environmental, and operational efficiency metrics to determine a

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1 corporate funding pool. American Water's program requires the [BEGIN  
2 CONFIDENTIAL] [REDACTED]  
3 [REDACTED] [END CONFIDENTIAL] to ensure the financial viability of the  
4 plan before any short-term variable compensation payment can be made to any  
5 participant.

6 American Water's short-term program design is within the range of market practice  
7 for utilities. Specific details regarding our assessment are included in Schedule  
8 RVM-1.

9 **25. Q. How does NJAWC's balanced scorecard approach to short-term at-risk pay**  
10 **benefit customers?**

11 A. The approach that NJAWC uses reflects a balanced approach between financial  
12 [BEGIN CONFIDENTIAL] [REDACTED] [END CONFIDENTIAL] and operational  
13 metrics [BEGIN CONFIDENTIAL] [REDACTED] [END CONFIDENTIAL]. While  
14 operational metrics may appear to reflect a more direct benefit to customers, the  
15 financial measures used in the short-term and long-term at-risk compensation  
16 programs send a message to employees that responsible financial stewardship is also  
17 important to the Company and its stakeholders, including customers. Strong financial  
18 performance enables the Company to invest in resources – both physical and people –  
19 that ensure the efficient operation of the Company, which benefits customers.

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**VII. SUMMARY OF WILLIS TOWERS WATSON'S LONG-TERM AT-RISK  
PROGRAM ASSESSMENT**

**26. Q. Did you conduct an assessment of American Water's long-term at-risk program?**

A. Yes.

**27. Q. What was the purpose of your assessment?**

A. This assessment was completed to compare the design of American Water's long-term at-risk program (that is applicable to NJAWC) and its various elements to market practice.

**28. Q. What were the findings of your assessment?**

A. Overall our review indicates that American Water's long-term at-risk program is comparable to and competitive with designs of utility peers, based on a review of the Large Utility Peer Group and the Small Utility Peer Group referenced earlier. Like American Water, every company in the Large Utility Peer Group and the Small Utility Peer Group has a long-term at-risk compensation program which is used to help attract, motivate and retain key senior level employees needed to successfully run the business. Companies design their long-term at-risk compensation programs to align with their business strategies and circumstances, so there tends to be a range of practices regarding how the programs are designed. American Water's long-term at-risk compensation program design is within the range of market practice for utilities. Specific details regarding our assessment are included in Schedule RVM-1.



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**VIII. OVERALL FINDINGS REGARDING NJAWC'S COMPENSATION PROGRAMS**

**29. Q. What are the overall findings and conclusions of your analysis of the compensation of NJAWC?**

A. Overall, our analysis indicates that NJAWC's total direct compensation programs are comparable to and competitive with market practices of other similarly-sized utilities and are therefore reasonable. NJAWC, like the companies it competes with for talent, has to provide a competitive total direct compensation opportunity delivered via programs that benefit employees, customers and shareholders. NJAWC attempts to achieve this goal with its balanced and competitive base salary and short-term and long-term at-risk compensation programs. My experience working with both utilities and general industry companies, and the results of the study included as Schedule RVM-1, indicate the programs at NJAWC are within a broad range of market norms and are not excessive in design or level of compensation.

**30. Q. Why is at-risk compensation appropriate for a utility?**

A. First, as our competitive assessment shows, the inclusion of at-risk plans, both short-term and long-term focused plans, is an essential part of a market competitive pay mix. As noted earlier in my testimony, all of the companies in the Large and Small Utility Peer Groups have short-term and long-term at-risk compensation plans in place. In order to attract, retain and motivate the talent needed to successfully run the company, NJAWC needs to provide a market competitive compensation program, which includes both short-term and long-term at-risk compensation plans.

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1 **31. Q. Describe the benefits of NJAWC's current compensation program in**  
2 **comparison to a base salary/wage-only approach.**

3 A. A key benefit of NJAWC's use of short-term and long-term at-risk compensation  
4 plans is that they align with competitive market practice and thereby enable NJAWC  
5 to compete in the market for talent. A shift to an all base salary program for NJAWC  
6 could have unintended consequences. If all or part of the short-term and/or long-term  
7 at-risk compensation at NJAWC were eliminated, the Company would likely be  
8 forced to increase fixed pay (i.e., base salary) to above market competitive levels in  
9 order to attract and retain talent. This would be counter to the pay-for-performance  
10 approach NJAWC currently employs, which is to put short-term and long-term  
11 compensation "at risk." At-risk compensation plans allow NJAWC to differentiate  
12 pay based on performance and allocate compensation to the highest performing and  
13 most deserving employees.

14 **32. Q. If NJAWC added target short-term at risk compensation to base salary, would**  
15 **NJAWC's total direct compensation remain competitively reasonable?**

16 A. Yes, it would remain in a competitively reasonable range.

17 **33. Q. How did you arrive at this conclusion?**

18 A. As shown in exhibits 2 and 3, the absence of short-term at-risk compensation would  
19 place NJAWC below competitive levels from a total compensation perspective. By  
20 adding it to base salary instead of eliminating it, the total program aligns with market  
21 median from a perspective of competitive pay levels.

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1   **34. Q. If companies do away with short-term at-risk but want to stay competitive,**  
2       **would they add short-term at-risk compensation to base salary?**

3       A. In my experience, companies would typically add 70% to 100% of the target short-  
4       term at-risk compensation to base salary depending on performance, payout history  
5       and the competitiveness and the risk profile of the program.

6   **35. Q. Would you recommend that a company do this?**

7       A. No, I would not.

8   **36. Q. Why would you recommend against it?**

9       A. While the level of compensation would be competitively reasonable, the program  
10      design would not be aligned with market and would be counter to the pay for  
11      performance objectives of the compensation program. This would reduce the reward  
12      potential for employees who distinguish themselves from a performance perspective  
13      in support of the company's mission and objectives. As discussed earlier in my  
14      testimony, every company reviewed from a program design perspective has short-  
15      term at risk compensation.

16   **37. Q. Does this conclude your testimony?**

17      A. Yes.

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**2017 General Rate Case Total Direct Compensation Study**

**New Jersey American Water Company**

September 11, 2017